

FACTORS AFFECTING QUALITY OF PROFIT IN MANUFACTURING COMPANIES LISTED IN INDONESIA STOCK EXCHANGE

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Abstract: The purpose of this study is to find out and analyze the factors that influence earnings quality in manufacturing companies listed on the Indonesia Stock Exchange. The dependent variable in this study is Profit Quality. Capital Structure, Liquidity, Sales Volatility and Operating Cycles as independent variables and company size as moderating variables. The object of this research is manufacturing companies listed on the Indonesia Stock Exchange in 2015-2018. The sampling technique uses purposive sampling method. The research sample consisted of 72 companies with 288 units of observation. Data analysis method is secondary data using Eviews 9. The results of this study indicate that capital and liquidity structures have a positive and significant effect on earnings quality. Sales volatility and operating cycles have a negative and significant effect on earnings quality. Company size variable is able to moderate the effect of capital structure and operating cycle on earnings quality while company size is not able to moderate the effect of liquidity and sales volatility.

Keywords: Capital structure, liquidity, sales volatility, operating cycle, earnings quality.

1. INTRODUCTION

Financial statements are the main tool for managers to demonstrate the effectiveness of achieving goals and to carry out the function of accountability in the organization. Information in the financial statements can help the owner or other parties such as creditors and investors to assess the company's strength in generating future profits. One indicator to assess a level of value the company has good or bad prospects in the future is to look at the company's ability to generate profits. Profit is used by external parties as an indicator to measure the company's operational performance. Earnings quality is the center of attention for users of financial statements, especially those who expect high quality earnings. Schipper and Vincent (2003) explain that earnings quality is used by investors and creditors as a basis for economic decision making, especially those relating to contracting decision making, investment decision and is used as an indicator of the quality of earnings generated standard setters. Penman (2001), revealed that quality earnings are earnings that can reflect the sustainability of earnings (sustainable earnings) in the future determined by the accrual component and its cash flow.

Libby and Libby (2009) in their book stated that the company's ability to generate cash from operating and management results for current assets and current liabilities is very important. Information on how much profit a company receives from operating activities can generate cash is very important for investors, creditors, and the management of the company itself. The greater the gap between

the profits generated and the cash flow of the company's operational activities, the less likely the company to be able to produce quality profits to meet their operational needs.

Capital structure is an illustration of the form of corporate financial proportion, which is between owned capital sourced from long-term liabilities and shareholders' equity which is the source of financing for a company. Leverage is a measurement commonly used for capital structure, because it is to determine the company's ability to use its assets and sources of funds financed by company debt. If the company has a high level of debt, the company will have increasingly large funds to develop the business and expand its business.

Liquidity is a financial ratio that measures a company's ability to meet short-term obligations with its current assets. The commonly used liquidity ratio is the current ratio. A high current ratio is usually considered to indicate there is no problem in liquidity, so the higher liquidity means that the profit generated by a quality company because company management does not need to practice earnings management.

Sales Volatility can also affect the quality of corporate earnings. Low volatility of sales will be able to show earnings ability in predicting future cash flow. However, if the level of sales volatility is high, then the quality of the profit will be low, because the profit generated will contain a lot of perceived noise.

The operating cycle is directly related to the company's profit, this is because there is a sales cycle operating factor. This profit will be used to predict future cash flows. Therefore, profits which are used to predict future cash flows, must really be quality earnings. Where the quality of profit itself depends on the operating cycle of the company itself.

The size of the company is the size of a company. The size of the company will be related to the quality of the company's earnings because the larger the size of a company, then the company has a higher business continuity, the performance of the company's management is better so that it is less likely to take earnings management actions.

2. THEORETICAL BASIS

According to Jensen and Meckling (1976) agency theory is a contract in which one or more people (principals) involve other people (agents) to perform a service on behalf of the principal and authorize the agent to make the best decision for the principal. The owner of the company (the principal) gives authority to the management (agent) to manage the company in order to generate high profits. In reality there is a possibility that management will not act in the best interests of the owner to maximize their own welfare. This can lead to a conflict of interest between management (agent) and company owner (principal).

Agency theory underlies the importance of analyzing the quality of earnings reported by the company as manager (agent) of the company's owner (principal). Supervision needs to be carried out on the financial statements made by management as a result of their performance. This is what underlies the importance of paying attention to the quality of earnings generated by company management

by analyzing the things that can affect the quality of earnings reported by the company.

A signal or signal according to Brigham and Houston (1999) is an action taken by company management, which gives instructions to investors about how management views the company's prospects. Signal theory explains that quality earnings can provide a positive signal for company stakeholders. Quality profits will be responded positively by the market and external parties will trust the company's management performance. This trust makes investors interested in investing capital in companies that can be used to develop businesses and increase profits.

Bellovary et al., (2005) in Surifah (2010) defines earnings quality as the ability of earnings to reflect the truth of a company's earnings and help predict future earnings, taking into account the stability and persistence of earnings. Penman (2001) states that quality earnings are earnings that can reflect the sustainability of earnings (sustainable earnings) in the future determined by the accrual component and cash flow. Dechow and Schrand (2004) revealed that quality earnings should be able to reflect the company's current operational performance, be an indicator of a company's good operational performance in the future, and be accurate in predicting the company's intrinsic value.

Capital structure is an illustration of the form of corporate financial proportions, namely between owned capital sourced from long-term debt (long term liabilities) and equity capital (shareholders equity) which is a source of financing for a company. Capital structure measured by leverage is a variable to find out how much the company's assets are financed by the company's debt

Liquidity Ratios are used to measure how liquid a company is by comparing all components in current assets with components in current liabilities (short-term debt). This ratio also shows the company's ability to pay its short-term debts (liabilities) that are due.

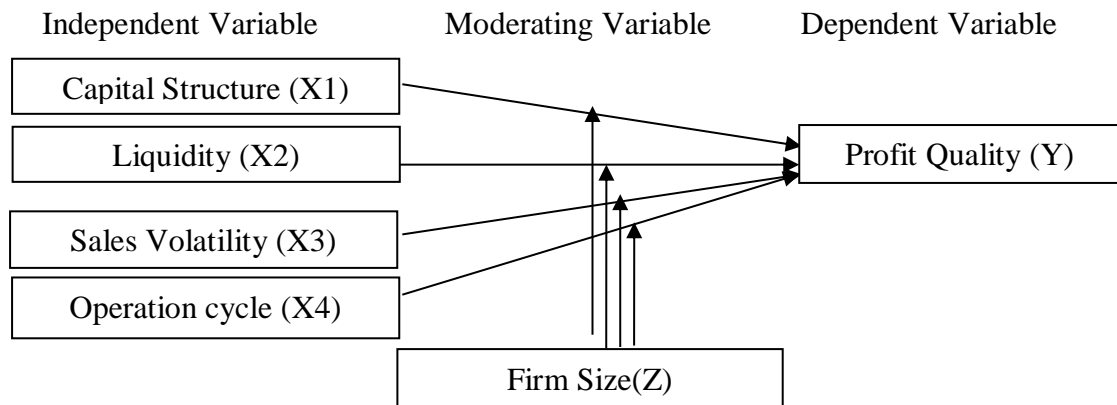
Sales volatility is the degree of spread of sales or the distribution index of the company's sales distribution (Dechow and Dichev, 2002). Sales volatility indicates a volatility of the operating environment and greater deviation of approximation and estimation, and corresponds to greater estimation errors and low quality accruals (Dechow and Dichev, 2002).

The operating cycle can be interpreted as the average time period between the purchase of inventory and cash collections that the seller will later receive. Or a whole series of transactions where a business generates receipts and cash receipts from customers. The operating cycle is directly related to the company's profit, this is because there is a sales cycle operating factor. This profit will be used to predict future cash flows.

Company size is the size of a company that can be classified based on various ways, including the size of revenue, total assets, and total equity (Brigham and Houston, 2001). According to Siregar and Utama (2006) the larger the size of the company, usually the information available to investors in making decisions regarding investment in the company's shares more and more.

3. CONCEPTUAL FRAMEWORK AND HYPOTHESES

Referring to several previous studies, the conceptual framework in this study consists of several factors that can affect earnings quality, namely capital structure, liquidity, sales volatility and operating cycles and company size as a moderating variable. Based on the description above, it can be made a conceptual framework model as shown below:



Based on the conceptual framework, the research hypothesis is as follows:

- H1: Capital structure has a positive effect on the quality of earnings in the company.
- H2: Liquidity has a positive effect on the earnings quality of the company.
- H3: Sales volatility has a negative effect on the earnings quality of the company.
- H4: Operating Cycle negatively affects the quality of earnings in the company.
- H5: Firm size can moderate the relationship between capital structure and company earnings quality.
- H6: Company size can moderate the relationship between liquidity and the company's profit quality.
- H7: Firm size can moderate the relationship between sales volatility and company earnings quality.
- H8: Company size can moderate the relationship between the operating cycle and the company's profit quality.

4. RESEARCH METHODS

This type of research is causal associative research. The relationship tested in this study is a partial and simultaneous relationship between the independent variables of capital structure, liquidity, sales volatility and operating cycles to the dependent variable of earnings quality and firm size as a moderating variable. The population in this study are all manufacturing companies listed on the Indonesia Stock Exchange from 2015 to 2018, amounting to 157 companies. The sample selection uses a purposive sampling method to obtain 72 companies. The year of observation was 4 years so the total number of observation units was 288.

The data analysis method used in this study is the method of statistical analysis of multiple linear regression using Eviews 9 software.

5. RESEARCH RESULTS AND DISCUSSION

5.1. Research Result

Based on data obtained from the financial statements of manufacturing companies which are the research samples, the descriptive statistics in this study can be shown in Table 1 as follows:

Table 1 Descriptive Statistics

	Y (QI)	Capital Structure	Liquidity	Sales Volatility	Operation Cycle	Firm Size
Mean	0.400208	-0.854236	0.780729	-2.106424	4.935556	15.11899
Median	0.225000	-0.875000	0.760000	-2.125000	4.995000	14.77000
Maximum	5.180000	6.470000	3.590000	3.100000	6.160000	23.04000
Minimum	-4.120000	-8.110000	-6.580000	-4.350000	3.180000	10.42000
Std. Dev.	1.322798	1.446233	1.042022	0.833032	0.524866	1.870637
Observations	288	288	288	288	288	288

Based on the results of the Chow test, it is known that the probability value is 0,000. Because the probability value is $0,000 < 0.05$, the estimation model used is the Fixed Effect Model (FEM). Furthermore, based on the results of the Hausman test, it is known that the probability value is 0.0563 because the probability value is $0.0563 > 0.05$, then the estimation model used is the Random Effect Model (REM). Furthermore, using the Lagrange-Multiplier test it is known that the P value of the Breusch-Pagan Cross-section value is 0,000 which is smaller than 0.05 ($0.000 < 0.05$), then the estimation model used is the Random Effect Model (REM).

Based on testing the hypothesis of the coefficient of determination, it is known that the coefficient of determination (Adjusted R-squared) of R^2 is 0.136. This value can be interpreted as Capital Structure, Liquidity, Sales Volatility and Operating Cycles simultaneously or jointly affecting the Profit Quality of 13.6%, the remaining 86.4% is influenced by other factors. The results of the F test, the Prob value is known. (F-statistics), which is $0,000 < 0.05$, it can be concluded that all independent variables, namely Capital Structure, Liquidity, Sales Volatility and Operation Cycle simultaneously have a significant effect on ROA variables.

Based on the t test, obtained capital structure has a significance value of t of $0.0000 < 0.05$, meaning that the capital structure partially has a significant effect on earnings quality. Liquidity has a significance value of t of $0.0002 < 0.05$, meaning that liquidity partially has a significant effect on earnings quality. Sales volatility has a significance value of t of $0.0148 < 0.05$, meaning that partial sales volatility has a significant effect on earnings quality. And the last operating cycle which has a significance value of t is $0.0010 < 0.05$, so the operating cycle has a significant effect on earnings quality partially.

Table 2 Test results of the significance of Company Size in moderating the influence of Capital Structure, Liquidity, Sales Volatility and Operating Cycles on Profit Quality with Interaction Test

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	6.502727	2.877670	2.259720	0.0246
X1	0.334102	0.081145	4.117372	0.0001

X2	0.107953	0.132261	0.816208	0.4151
X3	-0.186062	0.122710	-1.516282	0.1306
X4	-1.684909	0.556089	-3.029929	0.0027
Z	0.054060	0.061785	0.874956	0.3824
X1Z	-0.000465	0.000206	-2.256865	0.0248
X2Z	0.002293	0.002224	1.031143	0.3034
X3Z	-0.001769	0.004374	-0.404542	0.6861
X4Z	0.000486	0.000227	2.142198	0.0330

- a. The significance value at X1Z is 0.0248 which is smaller than 0.05. These results indicate that company size can moderate the effect of capital structure on earnings quality in manufacturing companies listed on the Indonesia Stock Exchange.
- b. The significance value at X2Z is 0.3034 which is greater than 0.05. These results indicate that the size of the company cannot moderate the effect of liability on the quality of the profit on manufacturing companies listed on the Indonesia Stock Exchange.
- c. The significance value at X3Z is 0.6861 which is greater than 0.05. These results indicate that company size cannot moderate the effect of sales volatility on earnings quality at manufacturing companies listed on the Indonesia Stock Exchange.
- d. The significance value at X4Z is 0.0330 which is smaller than 0.05. These results indicate that company size can moderate the effect of the operating cycle on earnings quality on manufacturing companies listed on the Indonesia Stock Exchange.

6. CONCLUSIONS

Based on the results of research and hypothesis testing that has been done, several conclusions can be drawn as follows:

1. Partially, capital structure has a positive and significant effect on earnings quality, so any increase in capital structure will encourage an increase in earnings quality.
2. Partially liquidity has a positive and significant effect on earnings quality, so any increase in liquidity will encourage an increase in earnings quality.
3. Sales volatility has a negative and significant impact on earnings quality, so any increase in sales volatility will drive down earnings quality.
4. The operating cycle has a negative and significant effect on earnings quality, so any increase in the operating cycle will lead to a decrease in earnings quality.
5. The moderating test results show that company size is able to moderate the effect of capital structure on earnings quality.
6. The moderating test results indicate the size of the company is not able to moderate the effect of liquidity on earnings quality.

7. The moderating test results indicate the size of the company is not able to moderate the effect of sales volatility on earnings quality.
8. The moderating test results indicate the size of the company is able to moderate the effect of the operating cycle on earnings quality.

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